

AUDITING PROCEDURES REPORT

Issued under P.A. 2 of 1968, as amended. Filing is mandatory.

Local Government Type <input type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input checked="" type="checkbox"/> Other		Local Government Name City of Kalamazoo Employees Retirement System	County Kalamazoo
Audit Date December 31, 2004	Opinion Date May 5, 2005	Date Accountant Report Submitted to State: June 23, 2005	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

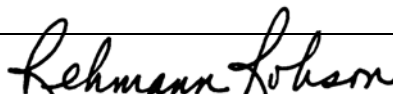
1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- | | |
|---|---|
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit. |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241). |
| <input type="checkbox"/> Yes <input checked="" type="checkbox"/> No | 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95). |

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.			X
Reports on individual federal financial assistance programs (program audits).			X
Single Audit Reports (ASLGU).			X

Certified Public Accountant (Firm Name) REHMANN ROBSON GERALD J. DESLOOVER, CPA			
Street Address 5800 GRATIOT, PO BOX 2025	City SAGINAW	State MI	Zip 48605
Accountant Signature 			

**CITY OF KALAMAZOO
EMPLOYEES' RETIREMENT SYSTEM**

**Financial Statements
And
Supplementary Information**

**For The Years Ended
December 31, 2004 and 2003**



REHMANN ROBSON

Certified Public Accountants

**CITY OF KALAMAZOO
EMPLOYEES' RETIREMENT SYSTEM**

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REHMANN ROBSON

Certified Public Accountants

A member of THE REHMANN GROUP



INDEPENDENT AUDITORS' REPORT

May 5, 2005

Members of the Employees'
Retirement System Investment Committee
City Commission of Kalamazoo
Kalamazoo, Michigan

We have audited the accompanying statements of plan net assets of the *City of Kalamazoo Employees' Retirement System* as of December 31, 2004 and 2003, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of the City of Kalamazoo. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements present only the Employees' Retirement System pension trust fund and do not purport to and do not present fairly the financial position and changes in financial position of the City of Kalamazoo, Michigan, in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of the City of Kalamazoo Employees' Retirement System as of December 31, 2004 and 2003 and the changes in plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The City has not presented Management's Discussion and Analysis for the Employees' Retirement System pension trust fund as required supplementary information. The GASB has determined that such information is necessary to supplement, although not required to be part of the financial statements.

The historical pension information listed in the table of contents is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and do not express an opinion on it.

Our audits were made for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying supplemental schedule of cash and investments as of December 31, 2004 and 2003, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the financial statements of the System. Such information has been subjected to the auditing procedures applied in our audits of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

A handwritten signature in black ink, reading "Lehmann Lobson". The signature is written in a cursive, flowing style with a large initial 'L'.

FINANCIAL STATEMENTS

CITY OF KALAMAZOO, MICHIGAN
Employees' Retirement System
Statements of Plan Net Assets
December 31, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Assets		
Cash and short-term investments	\$ 11,957,513	\$ 27,241,503
Receivables:		
Investments sold but unsettled	-	3,514,000
Interest and dividends	1,521,449	905,938
Investments:		
Government obligations	81,952,788	50,232,656
Corporate bonds	19,138,806	33,844,731
Corporate stocks	48,091,730	42,587,038
Equity mutual funds	266,941,715	242,236,351
Real estate mutual funds	22,511,133	20,032,548
	<u>438,636,172</u>	<u>388,933,324</u>
Total investments	<u>438,636,172</u>	<u>388,933,324</u>
 Total assets	 452,115,134	 420,594,765
 Liabilities		
Accounts payable for investments purchased but not settled	<u>1,542,212</u>	<u>14,127,065</u>
 Net assets held in trust for pension benefits (a schedule of funding progress is presented on page 10)	 <u><u>\$ 450,572,922</u></u>	 <u><u>\$ 406,467,700</u></u>

The accompanying notes are an integral part of these financial statements.

CITY OF KALAMAZOO, MICHIGAN
Employees' Retirement System
Statements of Changes in Plan Net Assets
For the Years Ended December 31, 2004 and 2003

	<u>2004</u>	<u>2003</u>
Additions		
Investment income:		
Net change in fair value of investments	\$ 48,961,400	\$ 85,756,705
Interest and dividends	9,131,878	6,832,743
Less investment advisor fees	<u>(1,568,290)</u>	<u>(832,182)</u>
Net investment income	56,524,988	91,757,266
Contributions - employees	<u>1,517,175</u>	<u>1,477,702</u>
Total additions	<u>58,042,163</u>	<u>93,234,968</u>
Deductions		
Pension benefits paid directly to participants	13,400,871	12,206,053
Refund payments to terminated employees	154,162	184,431
Trustee fees	207,798	210,332
Actuarial fees	32,734	36,216
Administrative fees paid to the City of Kalamazoo	97,770	89,600
Investment committee expenses	19,424	17,832
Other expenses	<u>24,182</u>	<u>19,966</u>
Total deductions	<u>13,936,941</u>	<u>12,764,430</u>
Net increase	44,105,222	80,470,538
Net assets held in trust for pension benefits		
Beginning of year	<u>406,467,700</u>	<u>325,997,162</u>
End of year	<u><u>\$ 450,572,922</u></u>	<u><u>\$ 406,467,700</u></u>

The accompanying notes are an integral part of these financial statements.

CITY OF KALAMAZOO

Employees' Retirement System

Notes To Financial Statements

1. PLAN DESCRIPTION

The City of Kalamazoo Employees' Retirement System (the "System") is a single-employer defined benefit contributory retirement plan which provides pension, death and disability benefits covering all full-time employees and some part-time employees of the City of Kalamazoo (the "City").

System membership consisted of the following at December 31, 2004 and 2003, the dates of the latest actuarial valuations:

	<u>2004</u>	<u>2003</u>
Retirees and beneficiaries currently receiving benefits	709	695
Terminated employees entitled to but not yet receiving benefits	28	34
Vested and non-vested active participants	<u>812</u>	<u>817</u>
Total	<u>1,549</u>	<u>1,546</u>

Plan members are required to contribute between 1.0% to 6.5% of their annual covered salary to the System for pension benefits, depending on bargaining unit. The City contributes such additional amounts, as necessary, based on actuarial determinations, to provide assets sufficient to pay for member benefits. No employer contributions were required for the years ended December 31, 2004 and 2003.

The System is administered by the City of Kalamazoo Employees' Retirement System Pension Board of Trustees. Plan benefit provisions were established and may be amended under the authority of City Ordinances. Employee contribution requirements were established and may be amended subject to collective bargaining agreements and approval by the City Commission of the City of Kalamazoo.

CITY OF KALAMAZOO

Employees' Retirement System

Notes To Financial Statements

2. SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting - The System's financial statements are prepared on the accrual basis of accounting. Member contributions are recognized in the period in which they are due. The City's contributions are recognized when due and the employer has made a formal commitment to provide them. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Valuation of Investments and Income Recognition - The System's investments are stated at fair value. Short-term investments are reported at cost, which approximates fair value. Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Mortgages are valued on the basis of future principal and interest payments, and are discounted at prevailing interest rates for similar instruments. The fair value of real estate investments is based on independent appraisals. Investments that do not have established market values are reported at estimated fair value.

Administration - Administrative costs are financed through the System's investment earnings.

3. CASH AND INVESTMENTS

Cash and short-term investments represent cash accounts held by the System's investment managers, and are insured by the Securities Investors Protection Act up to \$500,000 each. The carrying amount of these cash accounts as of December 31, 2004 and 2003 were \$11,957,513 and \$27,241,503, respectively, of which the insured amount was \$500,000. The remaining balances of \$11,097,513 and \$26,741,503, respectively, were uninsured and uncollateralized.

The System is authorized by the State's Pension Investment Act, as amended, to invest in common stocks, real estate, and various other obligations, subject to certain limitations. The System's common stock holdings accounted for 69.9% and 68.4% of the total investment portfolio (including short-term investment funds) at December 31, 2004 and 2003, respectively, which complies with the State statute limitation of 70%. There were no investments during the year in any one organization (other than the U. S. government) in excess of 5 percent of plan net assets.

CITY OF KALAMAZOO

Employees' Retirement System

Notes To Financial Statements

Investments are categorized for purposes of credit risk as either (1) insured or registered, or securities held by the government or its agent in the government's name, (2) uninsured or unregistered, with securities held by the counterparty's trust department or agent in the government's name, or (3) uninsured or unregistered, with securities held by the counterparty, or by its trust department or agent but not in the government's name.

The System's investment balances at December 31, 2004 and 2003, which were in category 3, except those indicated as uncategorized, were as follows:

	<u>2004</u>	<u>Fair Value</u>	<u>2003</u>
Government obligations	\$ 81,952,788		\$ 50,232,656
Corporate bonds	19,138,806		33,844,731
Corporate stocks	48,091,730		42,587,038
Investments not subject to categorization:			
Equity mutual funds	266,941,715		242,236,351
Real estate mutual funds	<u>22,511,133</u>		<u>20,032,548</u>
	<u>\$ 438,636,172</u>		<u>\$ 388,933,324</u>

The System's investment policy permits the prudent use of derivatives to reduce portfolio risk and enhance investment return. Under the terms of the investment agreements, portfolio managers are required to report all derivative holdings on a quarterly basis. The Investment Committee monitors these reports to evaluate the System's exposure to credit, market and legal risk.

The portfolios managed by Barclays Global Investors utilize certain derivatives, including futures, forwards and swaps. Also, the portfolios managed by Jennison Associates utilize mortgage derivatives. The System's share of the aggregate holdings in derivatives represented 2.5% of its investment in the Barclays portfolios, 39.6% of its investment in the Jennison portfolios and 10.36% of its total investments at December 31, 2004, and 25.4%, 1.3% and 6.9%, respectively, at December 31, 2003. During 2004 the value of derivatives held varied with market fluctuations and at times represented as much as 2.5% of its investment in the Barclays portfolios, 41.6% of its investment in the Jennison portfolio and 10.36% of its total investments.

CITY OF KALAMAZOO

Employees' Retirement System

Notes To Financial Statements

4. ANNUAL REQUIRED CONTRIBUTION

For both the years ended December 31, 2004 and 2003, the City had no required contributions, made no contributions and had no net retirement benefit obligation.

The annual required contributions for 2004 and 2003 were determined as part of an actuarial valuation of the System as of December 31, 2003 and 2002, respectively, using the individual attained age normal cost actuarial funding method. The actuarial assumptions included: (a) a nominal rate of return, net of expense, on investments of 7.5% per year compounded annually; (b) projected salary increases of 4.0% per year compounded annually, attributable to inflation; (c) additional projected salary increases ranging from 0.0% to 8.0% per year, depending on age and service, attributable to seniority/merit; and (d) the assumption that pension benefits will increase after retirement from 1.0% to 2.0% per year depending on the bargaining unit, age, and the date of retirement. The unfunded actuarial accrued liability is being amortized as a level percentage of payroll on an open basis. The remaining amortization period at December 31, 2004, was a rolling ten years for the System.

The actuarial value of assets was determined using techniques that smooth the effects of short-term volatility in the fair value of investments over a five-year period.

5. ADMINISTRATIVE EXPENSES

The following schedule identifies administrative expenses by type and percentage of net assets:

	<u>2004</u>		<u>2003</u>	
	<u>Amount</u>	<u>Percent of Net Assets</u>	<u>Amount</u>	<u>Percent of Net Assets</u>
Investment advisor				
fees	\$1,568,290	.348%	\$ 832,182	.205%
Trust and custodial fees	207,798	.046%	210,332	.052%
Administrative expenses	<u>174,110</u>	<u>.039%</u>	<u>163,614</u>	<u>.040%</u>
	<u>\$1,950,198</u>	<u>.433%</u>	<u>\$1,206,128</u>	<u>.297%</u>

CITY OF KALAMAZOO

Employees' Retirement System

Notes To Financial Statements

6. RISK MANAGEMENT

The System is exposed to various risks of loss related to torts, errors and omissions. The System participates in the City of Kalamazoo's risk management program for all of these exposures. The City's risk management program is primarily a self-insured program with reinsurance for amounts in excess of aggregate loss funds. The City estimates the liability for unpaid claims (including claims incurred but not reported) and allocates the cost to all appropriate entities and funds. There is no further exposure to the System that would require a liability to be recorded in the financial statements.

7. PENSION BENEFITS

During 2001, the City Ordinance was amended to provide for a supplemental benefits payment to certain retirees. Subject to certain limitations as described in the Ordinance, these payments may occur every third year commencing in 2001. Accordingly, the supplemental pension benefits for 2004 and 2003 amounted to \$747,869 and \$-0-, respectively.

* * * * *

**GASB REQUIRED
SUPPLEMENTARY INFORMATION**

CITY OF KALAMAZOO, MICHIGAN
Employees' Retirement System
Required Supplementary Information

Schedule of Funding Progress

Actuarial Valuation Date	Actuarial Value of Assets (A)	Actuarial Accrued Liability (B)	Overfunded AAL (OAAL) (A-B)	Funded Ratio (A/B)	Covered Payroll (C)	OAAL as a Percent of Covered Payroll
12/31/1995	\$ 180,374,616	\$ 139,177,079	\$ 41,197,537	129.6%	\$ 34,894,267	118.1%
12/31/1996	200,667,842	146,734,144	53,933,698	136.8%	34,888,439	154.6%
12/31/1997	242,709,209	161,366,282	81,342,927	150.4%	35,791,434	227.3%
12/31/1998	267,250,249	167,726,504	99,523,745	159.3%	35,607,350	279.5%
12/31/1999	303,750,495	192,167,206	111,583,289	158.1%	37,541,170	297.2%
12/31/2000	331,521,519	208,070,230	123,451,289	159.3%	39,377,238	313.5%
12/31/2001	349,206,708	220,302,430	128,904,278	158.5%	41,595,437	309.9%
12/31/2002	348,677,897	230,979,927	117,697,970	151.0%	40,316,918	291.9%
12/31/2003	361,205,383	245,919,424	115,285,959	146.9%	40,914,264	281.8%
12/31/2004	390,615,277	265,080,190	125,535,087	147.4%	41,989,819	299.0%

Schedule of Employer Contributions

Year Ended December 31	Annual Required Contributions	Percentage Contributed
1995	\$ 1,889,474	100%
1996	1,500,400	100%
1997	840,966	100%
1998	-	-
1999	-	-
2000	-	-
2001	-	-
2002	-	-
2003	-	-
2004	-	-

SUPPLEMENTARY INFORMATION

CITY OF KALAMAZOO, MICHIGAN
Employees' Retirement System
Schedule of Cash And Investments
December 31, 2004 and 2003

	Barclays Global Investors		Jennison Associates		Dimensional Fund Advisors, Inc.	
	Fair Value	Cost	Fair Value	Cost	Fair Value	Cost
<u>December 31, 2004</u>						
Investments						
Government obligations	\$ -	\$ -	\$ 81,952,788	\$ 78,633,575	\$ -	\$ -
Corporate bonds	-	-	19,138,806	17,451,236	-	-
Corporate stocks	-	-	-	-	-	-
Equity mutual funds	121,936,500	56,658,023	-	-	145,005,215	96,835,339
Real estate mutual funds	-	-	-	-	22,511,133	20,846,757
Total investments	121,936,500	56,658,023	101,091,594	96,084,811	167,516,348	117,682,096
Cash and short-term investment						
Short term investment funds	9	9	8,830,774	8,830,774	-	-
Total cash and investment:	\$ 121,936,509	\$ 56,658,032	\$ 109,922,368	\$ 104,915,585	\$ 167,516,348	\$ 117,682,096
<u>December 31, 2003</u>						
Investments						
Government obligations	\$ -	\$ -	\$ 50,232,656	\$ 49,501,473	\$ -	\$ -
Corporate bonds	-	-	33,844,731	32,881,490	-	-
Corporate stocks	-	-	-	-	-	-
Equity mutual funds	109,996,497	56,692,013	-	-	132,239,854	101,491,599
Real estate mutual funds	-	-	-	-	-	-
Total investments	109,996,497	56,692,013	84,077,387	82,382,963	132,239,854	101,491,599
Cash and short-term investment						
Short term investment funds	-	-	23,017,972	23,017,972	-	-
Total cash and investment:	\$ 109,996,497	\$ 56,692,013	\$ 107,095,359	\$ 105,400,935	\$ 132,239,854	\$ 101,491,599

Denver Investment Advisors, Inc.		Lend Lease		Master Account		Total	
Fair Value	Cost	Fair Value	Cost	Fair Value	Cost	Fair Value	Cost
\$ -	\$ -	\$ -	\$ -	-	-	\$ 81,952,788	\$ 78,633,575
-	-	-	-	-	-	19,138,806	17,451,236
48,091,730	37,951,575	-	-	-	-	48,091,730	37,951,575
-	-	-	-	-	-	266,941,715	153,493,362
-	-	-	-	-	-	22,511,133	20,846,757
48,091,730	37,951,575	-	-	-	-	438,636,172	308,376,505
1,507,536	1,507,536	-	-	1,619,194	1,619,194	11,957,513	11,957,513
<u>\$ 49,599,266</u>	<u>\$ 39,459,111</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 1,619,194</u>	<u>\$ 1,619,194</u>	<u>\$ 450,593,685</u>	<u>\$ 320,334,018</u>
\$ -	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 50,232,656	\$ 49,501,473
-	-	-	-	-	-	33,844,731	32,881,490
42,587,038	36,602,431	-	-	-	-	42,587,038	36,602,431
-	-	-	-	-	-	242,236,351	158,183,612
-	-	20,032,548	20,369,198	-	-	20,032,548	20,369,198
42,587,038	36,602,431	20,032,548	20,369,198	-	-	388,933,324	297,538,204
1,251,542	1,251,542	-	-	2,971,989	2,971,989	27,241,503	27,241,503
<u>\$ 43,838,580</u>	<u>\$ 37,853,973</u>	<u>\$ 20,032,548</u>	<u>\$ 20,369,198</u>	<u>\$ 2,971,989</u>	<u>\$ 2,971,989</u>	<u>\$ 416,174,827</u>	<u>\$ 324,779,707</u>